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April 3, 2002

Honorable Cris Andrews
Shasta County Assessor-Recorder
1500 Court Street, Suite 115
Redding, CA 96001-1694

Attn: Ms. Sandy Humphreys
Supervising Assessment Clerk

Re: *Change in Ownership - Nonprofit Mutual Benefit Corporation*

Dear Mr. Andrews:

This is in response to your October 8, 2001, letter to Chief Counsel Timothy Boyer wherein you advised that you received notification from the State Board Changes in Ownership of Legal Entities program (LEOP) concerning Fishing Club (Club), a nonprofit mutual benefit corporation, and its parcel of land in Shasta County, and you inquired concerning the change in ownership aspects of various transfers of interests in the property to the Club in 1990 and of subsequent transfers of membership interests in the Club among the original co-owners and to others thereafter. Your questions and our answers thereto follow.

1. In 1990, various persons transferred their interests in the real property to the Club. Was there a change in ownership of the property interests transferred?

Answer: The transfer of the interests in real property to the Club, a nonprofit mutual benefit corporation,¹ constituted a change in ownership under Revenue and Taxation Code section 60 and section 61, subdivision (i), now subdivision (j), unless an exclusion applied.

As you know section 60 provided then and continues to provide that a "change in ownership" means a transfer of a present interest in real property, including the beneficial use

¹ By letter dated November 17, 2001, you provided a copy of the Club's Articles of Incorporation, confirming the Club's status as a nonprofit mutual benefit corporation. Our analysis follows. You also forwarded a copy of the Club's 2001 By-Laws. They are not relevant for prior years in which changes in ownership occurred. By-laws, if any, in effect during those years would have to be obtained and reviewed to ascertain what effect, if any, they have upon the analysis in this letter.

thereof, the value of which is substantially equal to the value of the fee interest. Section 61, subdivision (i), now subdivision (j), provided that change in ownership, as defined in section 60, includes the transfer of any interest in real property between a corporation, partnership, or other legal entity and a shareholder, partner, or any other person.

Corporations Code sections 7110 et seq. provide for the creation of mutual benefit corporations, a type of nonprofit corporation recognized under that Code, which nonprofit corporations are treated as separate legal entities for property tax purposes. In general, as indicated in 15 Cal. Jur. 3d (Rev) section 699, mutual benefit corporations are formed principally for the mutual benefit of their members or for the mutual benefit of all those engaging in a particular type of business or activity. See pages 801-803 of 15 Cal. Jur. 3d (Rev.), copies enclosed.

Being a corporation for purposes of California law, the transfer of real property from individuals to a nonprofit mutual benefit corporation would be a change in ownership of the property within the meaning of section 60 and section 61, subdivision (i), unless an exclusion from change in ownership applies.

According to the December 10, 1990, copies of the deeds you provided, on that date 100 percent of the interests in the real property was transferred to the Club:

	<u>Transferor</u>	<u>Percentage Interest</u>
1	FB	10.66
2	MW	10.66
3	NB	3.55
4	TW	3.55
5	G	26.092
6	F	11.372
7	L	11.372
8	S	11.372
9	V	8.997
10	VIII	2.375
		<hr/> 100.00

Accordingly, such transfers resulted in a change in ownership of the real property within the meaning of section 60 and section 61, subdivision (i) at that time, apart from the application of an exclusion.

2. Was there any applicable exclusion from change in ownership in this instance?

Answer: Yes; there was probably an applicable exclusion from change in ownership, section 62, subdivision (a)(2).

Section 62, provided for exclusions from change in ownership. Section 62, subdivision (a)(2) provided:

62. Change in ownership shall not include:

(a)

X X X

(2) Any transfer between an individual or individuals and a legal entity or between legal entities, such as a cotenancy to a partnership, a partnership to a corporation, or a trust to a cotenancy, which results solely in a change in the method of holding title to the real property and in which proportional ownership interests of the transferors and transferees, whether represented by stock, partnership interest, or otherwise, in each and every piece of real property transferred, remain the same after the transfer. The provisions of this paragraph shall not apply to transfers also excluded from change in ownership under the provisions of subdivision (b) of Section 64.

We have previously stated that section 62, subdivision (a)(2) applies to transfers of real property to a nonprofit corporation when the transferors are the same individuals as the directors or members of the transferee nonprofit corporation after the transfer. See property tax annotation number 220.0081-C 8/5/83, copy enclosed.

Accordingly, if after the transfers of their interests in the real property, the persons transferring those interests in the real property held identical membership interests in the Club, section 62, subdivision (a)(2) would have been applicable, and the transfers of the interests in the real property to the Club would have been excluded from change in ownership pursuant thereto. Review of the Club's records would, no doubt, establish whether or not such was the case. In the event that after such transfers, the membership interests in the Club were not identical, such that section 62, subdivision (a)(2) was not applicable, absent any other exclusion from change in ownership, the 1990 transfers of the interests in the real property to the Club would have resulted in a 100 percent change in ownership of the property.

3. Was the County correct in applying section 62, subdivision (a)(2) to exclude the 1990 transfers of the interests in real property to the Club from change in ownership?

Answer: Yes, if as indicated in the answer to 2, above, review of the Club's records establishes that after the transfer of their interests in the real property to the Club, the persons holding those interests in the real property held the same membership interests in Club.

4. Did subsequent transfers of membership interests in the Club constitute changes in ownership that gave rise to reappraisal of those interests transferred?

Answer: Yes, based upon the information you have provided.

It has been unclear as to precisely what membership interests in the Club encompassed, interests in the corporation and the Club's real property or exclusive rights to occupy, use and enjoy specifically identifiable portions of the Club's real property. You recently advised, however, that the use of the property, land, a clubhouse, and two or three cabins, is available only to Club members on an all or partial use, informal, basis, as the members agree.² There are no exclusive rights of occupation and use of specifically identifiable portions of the Club's real property. Under the circumstances, the transfers of membership interests in the Club constituted transfers of real property interests in the Club's real property and changes in ownership of the real property interests transferred at the times of the transfers.³

In the past there was some question about whether a nonprofit mutual benefit corporation should be treated as a corporation and the members as shareholders, with the change in ownership consequences determined by the statutes and rule provisions for legal entities, or similar to a tenancy in common with the change in ownership consequences similar to those statutes and rule provisions pertaining to cotenants. As hereinafter indicated, we have been of the opinion that such corporations should be treated similar to tenancies in common, having change in ownership consequences similar to those of tenancies in common.

Following the adoption in 1978 of Proposition 13 (Article XIII A of the California Constitution) the Legislature adopted Part 0.5 (commencing at section 50) of Division 1 of the Revenue and Taxation Code, implementing the provisions of Article XIII A. Part 0.5 includes the provisions of Chapter 2 (commencing at section 60) concerning transfers resulting in changes in ownership and exclusions therefrom, including section 64 dealing with transfers of ownership interests in legal entities.

Subdivision (a) of section 64 provides the general rule that the purchase or transfer of ownership interests in a legal entity, such as corporate stock or partnership interests, shall not be deemed to constitute a transfer of the real property of the entity.⁴ The intent of the exclusion in section 64, subdivision (a) is to recognize the fact that "[s]hareholders of a corporation have no

possessory rights in corporate real property. Nor do partners – even in a general partnership – since their rights to partnership real property are limited to using the real property for partnership purposes.” (*Report of the Task Force on Property Tax Administration*, Assembly Revenue and Taxation Committee, January 1979, page 45.) Thus, pursuant to subdivision (a), transfers of ownership interests in a legal entity do not transfer interests in the real property owned by the legal entity because the holders of ownership interests have no possessory rights in that property.

² Such is consistent with the nature of a mutual benefit corporation, one formed principally for the mutual benefit of its members.

³ Had the interests in question been membership interests entitling members to exclusive rights to occupy, use, and enjoy specifically identifiable portions of the Club's real property, the transfers of those interests would similarly constitute changes in ownership of the portions of the real property transferred at the times of transfer. See our April 3, 2001, letter, upon which proposed property tax annotation number 220.0437 is based, to Honorable Gary W. Freeman regarding change in ownership - transfer of home site permits, copy enclosed.

⁴ Members of non-profit corporations have no ownership interests in the corporation that are equivalent to the ownership of stock interests.

Where, however, there is no stock ownership in instances involving nonprofit mutual benefit corporations, members of those corporations have possessory rights to the corporation's real property and are not limited to use of the corporation's real property for corporate purposes, the nature of the relationship for purposes of change in ownership is not that of a corporation and its shareholders but rather, that of a tenancy in common in which each co-owner's property interest is terminable and/or transferable. As membership interests in the Club give the members the rights to occupy, use, and enjoy the Club's real property and to transfer those rights,⁵ such interests comprise more than typical shareholders' interests in a corporation. Thus, as in the case of tenancy in common interests (Section 61, subdivision (f)), the creation, transfer or termination of membership interests in the Club should be changes in ownership of the interests transferred.

Proceeding in accordance with the above analysis, we further analyze the transfers in terms of the elements of change in ownership set forth in section 60. As observed in *Industrial Indemnity Co. v. City and County of San Francisco* (1990) 218 Cal.App.3d 999,1010, "The basic definition of section 60 is intended as a guidepost in cases not covered by the specific inclusions or exclusions of other taxation statutes or article XIII A itself." We think this principle applies here, where the character and detail of the transfers do not fit neatly into any of the statutory inclusions or exclusions found in sections 61 through 69.4.

Section 60 provides that

A "change in ownership" means a transfer of a present interest in real property, including the beneficial use thereof, the value of which is substantially equal to the value of the fee interest.

The first element of section 60 - the transfer of a present interest in real property - is satisfied here because the membership interests in the Club carry with them the present right, as opposed to a future right, to use and possession of the Club's real property. Moreover, an interest in property includes any one or various aggregates of rights, privileges, powers and immunities, the totality of which constitutes complete property, and a person who has all of these rights, privileges, powers and immunities is the owner of the property. (See Witkin, *Summary*, Ninth Edition, Real Property, § 3.) Thus, occupancy, use and enjoyment of the Club's real property by the members is a present interest therein.

The second element - the transfer of the beneficial interest - is also satisfied by the rights granted to each member. A beneficial interest is "[t]he right to use property and all that makes the property desirable or habitable . . . even if someone else owns the legal title to the property." (Blacks Law Dict. (7th ed. 1999) p. 1540.) Although the Club holds legal title to the property, each member has the right to occupy, use and enjoy the property or portions of it during the time he or she is a member, and the right to transfer his or her interest with regard to the property. The rights granted to members constitute the beneficial interests in the property, and transfers of such interests constitute transfers of beneficial interests therein.

⁵ Although not relevant, as indicated in Footnote 2, the Club's 2001 By-Laws set forth the members' rights, including the right to transfer membership interests and to receive pro-rata distributions upon the Club's dissolution.

Finally, the third element – the property interest must be substantially equal to the value of the fee interest - is satisfied by the specific rights granted to the members. The Task Force Report calls this element “the value equivalence test” and explains that it “is necessary to determine who is the primary owner of the property at any given time” and that its major purpose “is to avoid . . . unwarranted complexity by identifying the primary owner, so that only a transfer by him will be a change in ownership and when it occurs the whole property will be reappraised.” Similarly, in instances such as tenancies in common, it is necessary to determine who is the primary owner of the partial undivided ownership interests in the property at any given time. Thus, the primary owner or owners hold an undivided interest or interests that are substantially equal to the value of the fee interest and a transfer of such interest(s) is a change in ownership of the percentage interest(s) transferred. The members are the primary owners of the real property because they hold the rights most indicative of ownership, i.e., occupancy, use and enjoyment, and together the right to transfer the property or individually the right to transfer their respective portions of the property. (See Letters to Assessors No. 85/85 and No. 86/04.)

Thus, for example, when in 1991 FB transferred her undivided 10.66% interest in the Club, there was a 10.66% interest change in ownership of the Club's real property; when in 1991 also MW transferred her undivided 10.66% interest in the Club, there was another 10.66% interest change in ownership of the Club's real property; when in 1991 NB transferred a 3.55% interest in the Club, there was a 3.55% interest change in ownership of the Club's real property; when in 1991 TW transferred a 3.55% interest in the Club, there was a 3.55% interest change in ownership of the Club's real property; and when in 1992 G transferred her 11.8063% interest in the Club, there was a 11.8063 % interest change in ownership of the Club's real property.

Consistent with the conclusion that transfers of the membership interests result in changes in ownership, section 63 and section 63.1 are available to exclude such transfers between spouses and between parents and children and grandparents and grandchildren, assuming all other qualifications are met.

5. Did the transfer of membership interests in the Club to a seventh member (JW) in 1994 constitute a change in ownership that gave rise to reappraisal of those interests transferred?

Answer: Yes, for the same reasons explained in answer to Question 4 above.

The language in the 2001 Change in Control and Ownership of Legal Entities Statement filed for the Club suggests that the interest transferred was from the Club to a new member:

"In 1994 the Club issued a new (seventh) membership to J... W... for total consideration in the amount of \$125,000."

Unless the assessor had evidence to the contrary, the creation and transfer of an undivided one-seventh interest in the property would have resulted in a change in ownership of one-seventh of the Club's real property (presumably having a base year value of \$125,000). At the same time, the former members' 100% percent interest in the Club's real property would have decreased to a six-sevenths or 85.715% interest therein. Thus, for example, a member who had an undivided one-sixth or 16.67% interest in the Club's real property before JW

became a member would have had his or her interest reduced to a one-seventh or 14.285% interest when JW became a member.

In conclusion, you note that the Club is not currently filing for any type of exemption on the property. We would expect that this would be the case since, as indicated, mutual benefit corporations are formed principally for the mutual benefit of their members, whereas it is nonprofit public benefit corporations organized and operated for religious, hospital, or charitable purposes which are the types of corporations for which exemptions are available. (See Assessors' Handbook Section 267, "Welfare, Church and Religious Exemptions, Part I.)

The views expressed in this letter are only advisory in nature. They represent the analysis of the legal staff of the Board based on present law and the facts set forth herein. Therefore, they are not binding on any person or public entity.

Very truly yours,

/s/ James K. McManigal, Jr.

James K. McManigal, Jr.
Tax Counsel IV

Enclosures

JKM:lg

Precedent/Coowners/02/06jkm.doc

cc: Mr. David Gau, MIC:63
Chief, PPSD, MIC:64
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Ms. Jennifer Willis, MIC:70